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STATE FOR NEA/I, TREASURY FOR U/S ADAMS

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SUBJECT: IRAQ COMPACT: TREASURY DEPUTY SECRETARY MEETING
WITH KUWAIT FOREIGN MINISTER

REF: KUWAIT 4291

Classified By: Ambassador Richard LeBaron for reasons 1.4 (b) and (d)

11. (C) Summary: On October 31, Deputy Secretary of the Treasury Robert Kimmitt met with Kuwait Foreign Minister Shaykh Mohammed Sabah Al-Salem Al-Sabah on the margins of the International Compact for Iraq Preparatory Group (PG) meeting in Kuwait. Al-Sabah expressed little enthusiasm for debt forgiveness, noting that the Iraqis have substantial funds from donors that remain unspent. The meeting was also attended by Kuwait Fund Director General Abdulwahab Ahmed Al-Bader. End Summary.

12. (C) Kimmitt thanked the Minister for hosting the Iraq Compact meeting in Kuwait, noting the particularly symbolic nature of the event. The Government of Iraq, Kimmitt assured, wants to be financially independent in five years. Unfortunately, despite current aid levels, there is still a funding gap in the Iraqi budget. To help alleviate this gap, Kimmitt noted that the U.S. has already provided 100 percent debt forgiveness, and has provided and will continue to provide technical assistance, investment promotion support, and development and security assistance funding.

Debt Forgiveness: Amir Not Enthused By Forgiveness

13. (C) Providing a brief readout of the Iraqi delegation's meeting with the Kuwaiti Amir earlier in the day, Al-Sabah noted that Iraqi National Security Advisor Rubaie raised the issue of loan forgiveness. The Amir asked how forgiving debt would help the Iraqis, noting that Kuwait has already pledged \$500 million in development assistance and \$20 million in grants "but nothing has been spent." Al-Sabah asked Kimmitt if the disparity between the substantial, untouched pledges remaining and Iraq's continued request for additional aid "is a political message, because it does not translate." He stressed that the most important thing now is to see how Iraqis use the money that has already been pledged. (Note: In a later meeting with the Kuwait Fund Director General, Kimmitt asked the DG to inform Al-Sabah and the Finance Minister that \$75 million had already been disbursed.)

Debt Forgiveness: Too Sensitive

14. (C) Al-Sabah further cautioned that "loans are a very sensitive issue in Kuwait." He described internal political pressure from some members of the Parliament to write off loans of Kuwaiti private citizens, as "even more sensitive than the question of debt forgiveness in Iraq." For that very reason, Kimmitt noted, building consensus amongst GCC members and international creditors is crucial to creating a

political environment in Kuwait to address these sensitive but vital issues.

Not Just Budget, Or Corruption, But Security Too

15. (C) Kimmitt acknowledged that budget execution in Iraq continues to be problematic. He added, however, that the Iraqis have made some real progress as well, including the construction of many new schools. Kimmitt expressed hope that the PG will solidify Iraqis, sense of ownership of economic reform in Iraq. Although the Compact addresses a number of economic issues, he stressed that economic decisions can have a political effect. The Compact has become not only a key instrument through which Iraq is communicating with the international community, but it also provides impetus for making tough, but necessary, decisions. Without the pressure of the International Monetary Fund (IMF) standby agreement, Kimmitt continued, it would have been much more difficult for the Iraqis to make the progress seen thus far. The Iraqis "have shown their ability to make hard decisions in response to external pressures," he noted. Kimmitt told the FM he met with World Bank Representative Joe Saba on the eve of the ICI PG and noted a decided shift in his tone. Saba, who used to be more skeptical, said in the last three months he has seen a willingness to push forward projects and identify good people.

16. (C) Al-Sabah said that he understands that the Iraqis have a corruption problem but at the same time the capacity to use the funds that have already been pledged is not there. When dealing with Iraqis, he added, you must look at the incentive structure. The Iraqis promise good governance and transparency but movement on the security side is also

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required. "You read intel," he said, "you know of the involvement of Iran and the (situation with the) Shi'a in Central Iraq." An important development in this vein, Kimmitt responded, is the recognition that the support of Iraq's neighbors is vital.

The Way Ahead

17. (C) Foreign investment and access to capital markets, Kimmitt said, are the key to long-term success in Iraq. To achieve this, he explained, less debt is clearly better. Iraq has already begun trading its former commercial debt. Yet potential investors remain concerned about Iraq's ability to service its debt.

Reparations

18. (C) Kimmitt briefly commented on reparations from the 1990 invasion of Kuwait, noting that this is largely a bilateral issue. Al-Sabah said Kuwait was discussing with Iraq the idea of putting reparations into a central fund for projects in Iraq (e.g., environmental) that would benefit both countries. Kimmitt encouraged continuation of such discussions.

CTF/AML

19. (C) Kimmitt briefly noted that progress is being made on the counter-terrorist financing/anti-money laundering (CTF/AML) front. However, the more progress is made on the banking front the more people turn to informal means of transfer such as charities.

110. (U) This cable was cleared by Deputy Secretary Kimmitt.

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LeBaron